



## Internal Audit Report

**R.J Reynolds Tobacco Company**

*Company*

**Winston-Salem, North Carolina**

*Location*

**Sales and Distribution: Trade Marketing/Merchandising and Pricing/Distribution**

*Business Process*

**June 1, 1998**

*Issued*

**R98-003**

*Reference*

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**- Distribution -**

*Executive Summary Only*

**R.J. Reynolds Tobacco Company**

C.T. Hill  
J.V. Maguire  
B.K. Stockdale  
W.F. Tucker  
D.L. Wilmesher

**Deloitte & Touche**

New York  
Winston-Salem

**R.J. Reynolds Tobacco Company**

K.J. Lapiejko  
A.J. Schindler

**RJR Nabisco, Inc.**

L.L. Nowell, III  
D.B. Rickard  
R.G. Russell  
W.L. Rosoff

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Entity	Operating Company Business Objectives
R.J. Reynolds Tobacco Company  Winston-Salem, NC ("RJRT")	Ensure competitively positioned cost structure and alignment of resources, focusing on cost and process efficiencies and balancing marketplace investments for maximum return

Business Process/Sub-Process
Sales and Distribution: Trade Marketing / Merchandising and Pricing / Discounting

RAAP Objectives
Our audit, which was performed in April 1998, included an on-site visit to the New York Region (North East Sales Area) and covered the period of January through December 1997. We focused on the following objectives: <ul style="list-style-type: none"> <li>Assessing Region control activities relating to Trade Marketing and Merchandising and Pricing and Discounting sub-processes, including: <ul style="list-style-type: none"> <li>Contract Administration and Disbursements</li> <li>Pricing and Discounting Execution and Disbursements</li> </ul> </li> <li>Performing retail visits to assess execution of RJRT's Trade Marketing and Merchandising and Pricing and Discounting strategies</li> <li>Identifying opportunities to enhance operational processes</li> </ul>

Business Control Assessment	
Pricing / Discounting Execution and Disbursements	Controls functioning as intended
Contract Administration and Disbursements	Controls functioning as intended

Profile
<p>Within RJRT's four sales areas, 20 regions provide centralized, administrative support to Field Sales in executing display coverage, pricing and promotion strategies. The objective of these strategies is to improve share of market through price management and discounting, retail merchandising presence, and retail accrual tactics. RJRT's pricing strategy aims to maintain a defined price difference, a "price gap," between RJRT's core full price brands and competitive branded savings, while matching Marlboro. RJRT also defends Salem and matches Doral against key competitive discount brands up to specific levels. Pricing strategy is achieved through discounting the list price of product at retail. Retail merchandising presence comprises display and sale of RJRT products, supported by contracts between RJRT and retail accounts. Quarterly payments to retail accounts are based on the number and positioning of RJRT product displays, RJRT's sales volume in the account and competitive payment pressure for space.</p> <p>New York Region spent \$7.7 million on discounting and promotional payments from January 1, 1997 to December 30, 1997, while RJRT spent \$576.7 million. From 1/1/97 to 9/30/97, New York spent \$5.4 million on merchandising contract payments and RJRT spent \$202 million.</p>

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Internal Audit Team		Management Team	
Name	Title	Name	Title
Joanne Jacovec	Director, Internal Audit	Jim Maguire	Senior Vice President Sales
Karyl McClusky	Manager, Internal Audit	Craig Hill	Director, Sales Financial Services
Susan Baker	Senior Internal Auditor		
Tony Egbuna	Senior Internal Auditor		
Dan Michels	Senior Internal Auditor		
Anne Cullip	Guest Auditor, RJRT Sales Finance		

Management Accountability
Craig Hill, Director, Sales Financial Services will monitor any corrective action required.

June 1, 1998

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New York Region

**Pricing/Discounting Disbursements**

Activity Management

*Observation* Region Operations Manager is not reviewing and approving voucher requests over \$10,000.

*Recommendation and Expected Result* Review and approve all vouchers over \$10,000.

*Management Action*

*Observation* Newly assigned draft books are placed in unsecured mail slots for up to a day before being mailed.

*Recommendation and Expected Result* Secure all draft books until they are actually mailed.

*Management Action*

*Observation* At three different retailer accounts, product discounted at the wholesaler was not black marked by the wholesaler.

*Recommendation and Expected Result* Sales and Retail Reps ("SR" "RR") should follow up with the wholesaler to ensure all discounted product is being correctly marked. Any discounted product at retail which is not already marked should be marked by the SR or RR.

*Management Action*

*Observation* Two retail accounts contained product on display which had discounting stickers that have not been used in at least 8 months. The product appeared to be stale.

*Recommendation and Expected Result* Remind RR's and SR's to rotate product and remove all stale product.

*Management Action*

**Contract Administration and Disbursements**

Activity Management

*Observation* District Managers ("DM's") are not required to follow up on the monthly volume/contract exceptions report to ROU personnel.

*Recommendation and Expected Result* Require the DM's to respond to the ROU on all items on the monthly volume/contract exception report which are off by two or more grid levels.

*Management Action*

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